Testimony of Alan M. White

Valparaiso University School of Law

Before the House Committee on Financial Services

Hearing on the Implementation of the HOPE for Homeowners Program and a Review of Foreclosure Mitigation Efforts

September 17, 2008

Chairman Frank, Ranking Member Bachus, and members of the Committee, thank you for this opportunity to testify concerning the vital questions of how we are responding and should respond to the foreclosure crisis. I have studied the subprime mortgage industry for the past ten years, and I am currently researching mortgage defaults, foreclosures, workouts and modification agreements. At a Federal Reserve Board hearing in Boston on August 4, 2000, I testified that while high fees and frequent refinancings were a concern, mounting foreclosure rates were a bigger problem, and I urged the Federal Reserve to require reasonable determinations of repayment ability by subprime lenders. Before I moved to full-time teaching last year, I worked with hundreds of homeowners facing foreclosure as a legal services lawyer in Philadelphia, and negotiated dozens of loan modification agreements.

Today I will summarize my findings thus far on mortgage modifications during the last twelve months, suggest the need for a federal role in gathering and reporting information on mortgage foreclosure and workouts, and offer some observations on why mortgage servicers are not modifying mortgages more aggressively.

Given the stakes and the economic impact of foreclosures, there is surprisingly little reliable information about whether the Administration's plan to rely on voluntary industry-led measures is working. Policy makers and the public want to know answers to some basic questions: How much longer will record levels of foreclosures continue? Are we doing everything possible to avert preventable foreclosures? Are mortgage servicers offering appropriate restructuring terms to distressed homeowners, and are mortgage investors suffering needless losses on distress-price foreclosure sales? On the other hand, are homeowners simply delaying the inevitable, because payment plans and modification agreements are not working, which will lead to further defaults and losses?

To address the lack of information on mortgage modifications, I have begun collecting data from monthly remittance reports prepared by mortgage servicers for investors. These reports are generally not filed with the SEC, because of a rule that exempts securitizations with fewer than 300 investors from ongoing reporting. However, some mortgage servicers and trustees make these reports available on their web sites.

So far I have gathered information about 4,300 mortgage modifications made between July 2007 and June 2008, in a sample of 105,000 mortgages. The sample included nine of the top fifteen subprime mortgage lenders and eight of the top fifteen servicers. The loans were all originated in 2005 and 2006, and were predominantly hybrid adjustable-rate mortgages.

Thus, if the problems to be solved are: first, excessive total mortgage debt and second, payments that are not affordable, the first problem is almost never being solved, and the second is being redressed in only about half of the modifications offered.

At the same time, the urgent need for sustainable mortgage modifications grows every month. During the past twelve months the loss severities on completed foreclosures have increased from about 30% to almost 40% on average, meaning that investors are doing worse and worse by choosing the foreclosure option. At the same time, the ability of borrowers to refinance has steadily eroded, to the point where by June 2008 there were more foreclosure sales than refinancings.

Equally striking was the fact that the number and type of modifications varies tremendously from one servicer to another. Although the trustee was the same for all the mortgage pools I studied, there was no uniformity in the approach to workouts. Some servicers made significant principal and monthly payment reductions, while others offered only reamortizations that increased loan balances. During the twelve months in question, one servicer modified 2% of the delinquent mortgages in a pool, while another servicer modified 56% of the delinquent mortgages in one of its pools.

The complete paper detailing my findings is available on line at http://ssrn.com/abstract=1259538.

Although there is not much reliable data on how well borrowers do after their loans are modified, industry estimates on re-default rates seem to run at about 35% to 40%. While this seems high, it means that more than half of these homeowners are able to maintain their new payments, even without any significant principal reductions, and often without even a payment reduction. It seems intuitively obvious that more generous loan restructuring would produce better success rates. As for borrowers who are defaulting a second time, it is true that investors may suffer increased losses, but measuring those incremental losses, and comparing them with the savings from successful modifications and workouts, is a complex undertaking. In my view, the fact that 2007 loan modifications were not uniformly successful should not necessarily lead us to give up on more aggressive modifications as a solution to the crisis.

I would also like to address briefly the need for better public information gathering and reporting concerning the unfolding crisis. At present the public does not know the answers to basic questions about foreclosures and workouts, although the information exists. The Mortgage Bankers Association's quarterly National Delinquency Survey (NDS) comes out two months after the fact. While its coverage is comprehensive, the NDS provides the number of foreclosures started, and the number in process, but not the number of final foreclosure sales, or any information about foreclosure alternatives such as modification agreements. The HOPE NOW coalition releases monthly data in a more timely fashion, but does not cover the entire mortgage market, and while their reports do provide numbers of loan modifications, there is no information about the nature of those modifications, nor about whether they are successful, i.e. whether homeowners are remaining current on modified mortgages. The state agency Foreclosure Prevention Working Group has released two reports to date, with richer detail, but does not appear to be a regular and permanent source of public

TABLES AND FIGURES

Table 1

| Pool name | Originator | Servicer |
|---|---|---|
| ABFC 2005-OPT1 | Option One | Option One |
| ABFC 2006-OPT1 | Option One | Option One |
| ABFC 2006-OPT2 | Option One | Option One |
| ABFC 2006-OPT3 | Option One | Option One |
| Aames MIT 2005-4 | Aames Mortgage | Aames Funding |
| Aames MIT 2006-1 | Aames Mortgage | Aames Funding |
| ACE Securities 2006-CW1 | Countrywide | Countrywide |
| ACE Securities 2006FM-1 | Fremont | Fremont |
| First Franklin LT 2005-FF6 | First Franklin | First Franklin |
| FFLT 2006-FF1 | First Franklin | First Franklin |
| FFLT 2006-FF11 | First Franklin | First Franklin |
| Fremont HLTrust 2005A | Fremont | Fremont |
| Fremont HLTrust 2006A | Fremont | Fremont |
| HSIASC WMC2006-1 | WMC | Wells Fargo |
| JPMAC2006-CW2 | Countrywide | Countrywide |
| Merrill Lynch MIT 2006-1 | WMC | Wells Fargo |
| Park Place 2005WHQ1 | Argent/Ameriquest | HomEq |
| Park Place 2005 WHQ4 | Argent | HomEq |
| Renaissance HELT2006-1 | Delta | Ocwen |
| Renaissance HELT2005-1 | Delta | Ocwen |
| SASCO 2006BC6 | Various | Aurora |
| WFHET 2005-1 | Wells Fargo | Wells Fargo |
| WFHET 2005-2 | Wells Fargo | Wells Fargo |
| WFHET 2005-4 | Wells Fargo | Wells Fargo |
| WFHET 2006-2 | Wells Fargo | Wells Fargo |
| WFHET2006-3 | Wells Fargo | Wells Fargo |

Fig. 3

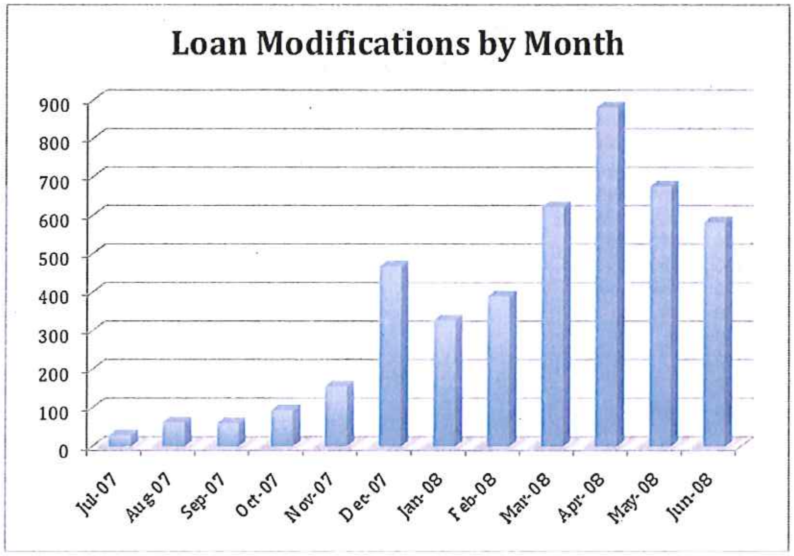
Loan Modifications by Month
900
800
700
600
500
400
300
200
100
0
Jul-07
Aug-07
Sep-07
Oct-07
Nov-07
Dec-07
Jan-08
Feb-08
Mar-08
Apr-08
May-08
Jun-08

Fig. 4

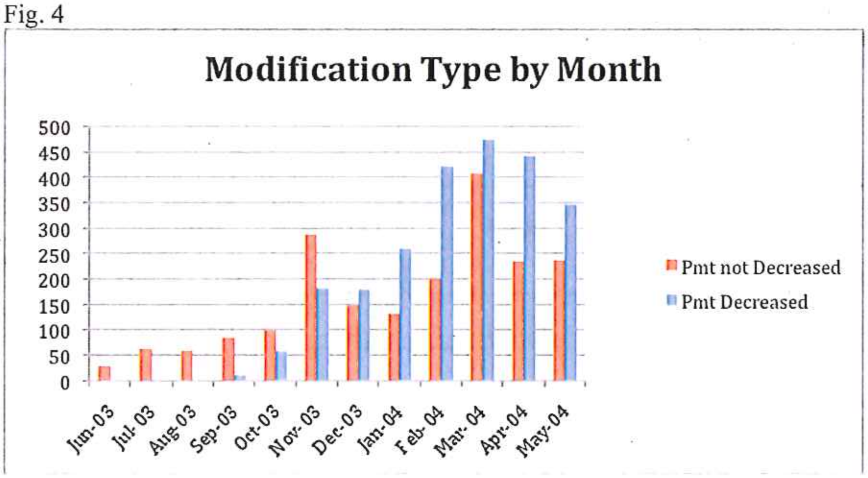
Modification Type by Month
500
450
400
350
300
250
200
150
100
50
0
Jun-03
Jul-03
Aug-03
Sep-03
Oct-03
Nov-03
Dec-03
Jan-04
Feb-04
Mar-04
Apr-04
May-04
Pmt not Decreased
Pmt Decreased

Table 3

**12 month totals, Modifications vs. Delinquent Loans and Liquidated Foreclosures**

| | *Liquidations* | *Modifications* | *Delinquent (Max)* | *Mods/Liquidations* | *Mods/Delinquents* |
|---|---|---|---|---|---|
| Aames MIT 2005-4 | 459 | 476 | 1140 | 103.70% | 41.75% |
| Aames MIT 2006-1 | 281 | 157 | 673 | 55.87% | 23.33% |
| ABFC 2005-OPT1 | 99 | 42 | 381 | 42.42% | 11.02% |
| ABFC 2006-OPT1 | 349 | 26 | 1196 | 7.45% | 2.17% |
| ABFC 2006-OPT2 | 212 | 43 | 1140 | 20.28% | 3.77% |
| ABFC2006-OPT3 | 132 | 65 | 867 | 49.24% | 7.50% |
| ACE Securities 2006-CW1 | 182 | 81 | 1159 | 44.51% | 6.99% |
| Ace Securities 2006-FM1 | 560 | 701 | 1689 | 125.18% | 41.50% |
| First Franklin MLT 2005-FF6 | 223 | 113 | 641 | 50.67% | 17.63% |
| First Franklin MLT 2006-FF1 | 538 | 294 | 2316 | 54.65% | 12.69% |
| First Franklin MLT 2006-FF11 | 381 | 129 | 2316 | 33.86% | 5.57% |
| Fremont HLT 2005A | 187 | 276 | 490 | 147.59% | 56.33% |
| Fremont HLT 2006A | 303 | 408 | 1084 | 134.65% | 37.64% |
| HISASC 2006-WMC1 | 554 | 142 | 1171 | 25.63% | 12.13% |
| JPMorganMAT 2006-CW2 | 213 | 67 | 1264 | 31.46% | 5.30% |
| Merrill Lynch MIT 2006-WMC1 | 742 | 352 | 1374 | 47.44% | 25.62% |
| Park Place 2005 WHQ1 | 621 | 1 | 1395 | 0.16% | 0.07% |
| Park Place 2005 WHQ4 | 585 | 0 | 1783 | 0.00% | 0.00% |
| Renaissance HELT 2005-1 | 68 | 155 | 537 | 227.94% | 28.86% |
| Renaissance HELT 2006-1 | 124 | 70 | 893 | 56.45% | 7.84% |
| SASCO 2006-BC6 | 230 | 47 | 1183 | 20.43% | 3.97% |
| Wells Fargo HET 2005-1 | 183 | 116 | 785 | 63.39% | 14.78% |
| Wells Fargo HET 2005-2 | 122 | 100 | 735 | 81.97% | 13.61% |
| Wells Fargo HET 2005-4 | 132 | 134 | 813 | 101.52% | 16.48% |
| Wells Fargo HET 2006-2 | 167 | 299 | 1226 | 179.04% | 24.39% |
| Wells Fargo HET 2006-3 | 180 | 177 | 1621 | 98.33% | 10.92% |